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ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION  
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JIM IRVIN  
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Commissioner

In the matter of:

STEPHEN MICHAEL JOHNSON  
(CRD #721408),  
d/b/a FERNDAL FINANCIAL GROUP,  
839 S. Westwood #245  
Mesa, Arizona 85210,  
Respondent.

DOCKET NO. S-03403A-01-0000

**NOTICE OF OPPORTUNITY FOR  
HEARING REGARDING PROPOSED  
ORDER TO CEASE AND DESIST,  
FOR ADMINISTRATIVE PENALTIES,  
OF REVOCATION, AND FOR  
OTHER AFFIRMATIVE ACTION**

**NOTICE: RESPONDENT HAS 10 DAYS TO REQUEST A HEARING**

The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") alleges that respondent has engaged in acts, practices and transactions that constitute violations of the Securities Act of Arizona, A.R.S. § 44-1801 *et seq.* ("Securities Act").

**I.**

**JURISDICTION**

1. The Commission has jurisdiction over this matter pursuant to Article XV of the Arizona Constitution and the Securities Act.

**II.**

**RESPONDENT**

2. Stephen Michael Johnson, CRD #721408, has been a registered securities salesman in Arizona since at least 1997. Johnson was associated with the following broker-dealer firms during the time period relevant to this Notice: Washington Square Securities, Inc. ("WSS") (1997), American General Securities Incorporated ("American General") (January – August 1998), New York Life Securities, Inc. (October 1998 – July 1999), LifeUSA Securities, Inc., which became

1 USAllianz Securities, Inc. (June 1999 – the present). Johnson has been doing business as Ferndale  
2 Financial Group (“Ferndale”) since at least December 1996. In this Notice, Ferndale and Johnson  
3 are collectively referred to as “Johnson.” At all times relevant to this Notice, Johnson has resided in  
4 Arizona. Johnson’s last known address is 839 S. Westwood #245, Mesa, Arizona 85210.

### 5 III.

### 6 FACTS

7 3. Between in or about August 1997 – June 1998, while he was registered with WSS or  
8 American General, Johnson doing business as Ferndale, offered or sold securities in the form of  
9 fractional, undivided interests in oil and gas rights and/or investment contracts. The securities took  
10 the form of membership interests in Petroleum Resources, L.L.C. (the “LLC”), an entity organized  
11 under the Utah Limited Liability Company Act.

12 4. Johnson offered or sold the securities from his home office and/or other locations in  
13 Arizona.

14 5. Johnson received compensation for offering and/or selling the securities, in the form of  
15 an ownership interest in the LLC. In addition, in or about February or March 1998 Johnson was  
16 paid \$2,000 as additional compensation from the LLC for his selling activity.

17 6. Johnson raised approximately \$500,000 in invested funds for the LLC, from six  
18 investors, of whom one was an Arizona resident.

19 7. The sales of LLC interests made by Johnson were not recorded on the books and  
20 records of the broker-dealer firm with which Johnson was associated at the time of the sales.

21 8. Johnson neither sought nor received approval from WSS or American General to offer  
22 or sell LLC interests. In addition, Johnson neither sought nor received approval from any of the  
23 broker-dealers with which he was associated, for his outside business activities with regard to the  
24 LLC, which continued until in or about September 1999.

25 9. The initial members of the LLC when it was organized were Johnson and The Shasta  
26 Trust, which was a front for William Robertson McRae (a/k/a “Peter” McRae). Johnson signed the

1 LLC's Articles of Organization as "president" and "manager," and he held himself out to the  
2 investors and others as "president," but he permitted McRae to exercise sole management control  
3 of the LLC from its organization date, on or about October 31, 1997, until in or about August 1998.

4 10. The business of the LLC was to operate oil and gas wells located in Oklahoma and  
5 Kansas pursuant to two leases, and to drill and develop additional wells pursuant to the leases.  
6 McRae contributed interests in the two leases to the LLC but retained a percentage interest in each  
7 lease, through entities that he controlled.

8 11. Johnson did not investigate McRae's background prior to beginning to offer and sell  
9 securities pursuant to his agreement with McRae. Had Johnson done so, he would have learned  
10 that in 1996 McRae and his wife, Barbara McRae, had consented to entry of a judgment prior to  
11 trial in a civil action that had been commenced by the Securities Division. That civil action  
12 concerned the fraudulent offer and sale of investments in oil and gas ventures to at least 95  
13 investors, in which over \$2 million had been lost. Pursuant to the 1996 consent judgment, the  
14 McRaes had been permanently enjoined from offering or selling any securities, from the date of the  
15 judgment forward. The McRaes had been further enjoined from committing securities fraud as  
16 defined in A.R.S. §44-1991, and from committing fraud in connection with the advertisement and  
17 sale of merchandise as defined in A.R.S. § 44-1552. In addition, the McRaes had been ordered to  
18 pay restitution in the amount of \$2,004,625 and a civil penalty of \$100,000.

19 12. Johnson took over control of the LLC from McRae and managed the LLC business,  
20 from in or about August 1998, to in or about September 1999. An investor board was constituted  
21 late in 1998, but Johnson remained the sole executive officer during this period, Johnson managed  
22 the day-to-day business of the LLC, and only Johnson's signature was required to write checks on  
23 the LLC account.

24 13. Between in or about March 1999 and September 1999, Johnson wrote several checks on  
25 the LLC account, which he cashed and used for personal expenses.  
26

1 14. Johnson concealed his use of LLC funds for personal expenses by, in at least one  
2 instance omitting to record the check in the LLC's ledger, and in several other instances recording  
3 a payee name in the ledger that was a real vendor to the LLC, but actually writing the check to the  
4 order of "cash" or to himself.

5 15. Johnson wrote the word "loan" on some of the checks, but did not provide the LLC with  
6 any documentation that he owed the LLC money, and he received these LLC funds without the  
7 knowledge of any of the investors.

8 16. In or about September 1999 one of the investors examined the LLC books and  
9 discovered Johnson's unauthorized uses of LLC funds. Thereafter the investors took over control  
10 of the LLC's business and bank account, and Johnson made a payment to the LLC of \$9,150.00.  
11 Johnson considered this payment to include restitution of the funds he had taken from the LLC as  
12 alleged in paragraphs 13 – 15, as well as a "loan" from himself to the LLC. The LLC documented  
13 the "loan" as a contribution to capital by Johnson.

14 17. Altogether the amount of money Johnson received from the LLC exceeded the amount  
15 of money he paid to the LLC, by approximately \$9,000.00.

16 **IV.**

17 **VIOLATION OF A.R.S. § 44-1841**

18 **(Offer or Sale of Unregistered Securities)**

19 18. Johnson offered or sold securities in the form of fractional, undivided interests in oil and  
20 gas rights and/or investment contracts, within or from Arizona.

21 19. The securities referred to above were not registered pursuant to Articles 6 or 7 of the  
22 Securities Act.

23 20. This conduct violates A.R.S. § 44-1841.

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V.

REVOCATION PURSUANT TO A.R.S. § 44-1962

(Denial, Revocation or Suspension of Registration of Salesman)

21. Johnson's conduct is grounds to revoke his registration as a securities salesman with the Commission pursuant to A.R.S. § 44-1962. Specifically, Johnson:

a) has engaged in conduct specified by A.R.S. §44-1962(A)(2) in that he violated a provision of the Securities Act by selling unregistered securities, as alleged above;

b) lacks integrity or is not of good business reputation as specified by A.R.S. §44-1962(A)(4) as evidenced by, in particular, his unauthorized and undocumented "borrowing" of LLC funds; and/or

c) has engaged in conduct specified by A.R.S. §44-1962(A)(10) and Ariz. Admin. Code R14-4-130(A)(17) -- specifically, effecting sales of securities that were not recorded on the records of the broker-dealer firm with which he was associated at the time of the sales.

VI.

REQUESTED RELIEF

The Division requests that the Commission grant the following relief against Johnson:

1. Order Johnson to cease and desist permanently from violating the Securities Act, pursuant to A.R.S. § 44-2032;

2. Order Johnson to pay the state of Arizona administrative penalties of up to five thousand dollars (\$5,000) for each violation of the Securities Act, pursuant to A.R.S. § 44-2036;

3. Order Johnson to take affirmative action to correct the conditions resulting from his acts, practices or transactions, including a requirement to make restitution pursuant to A.R.S. § 44-2032;

4. Order the revocation of Johnson's registration as a securities salesman pursuant to A.R.S. § 44-1962; and

5. Order any other relief that the Commission deems appropriate.

VII.

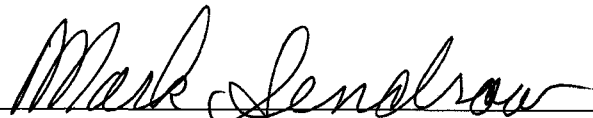
HEARING OPPORTUNITY

Johnson may request a hearing pursuant to A.R.S. § 44-1972 and Ariz. Admin.Code R14-4-306. A request must be in writing and received by the Commission within 10 business days after service of this Notice of Opportunity for Hearing. Johnson or his attorney must deliver or mail the request to Docket Control, Arizona Corporation Commission, 1200 W. Washington, Phoenix, Arizona 85007. A Docket Control cover sheet must accompany the request. A cover sheet form and instructions may be obtained from Docket Control by calling (602) 542-3477 or on the Commission's Internet web site at [www.cc.state.az.us/utility/forms/index.htm](http://www.cc.state.az.us/utility/forms/index.htm).

If a request for a hearing is timely made, the Commission shall schedule the hearing to begin 20 to 60 days from the receipt of the request unless otherwise provided by law, stipulated by the parties, or ordered by the Commission. If a request for a hearing is not timely made the Commission may, without a hearing, enter an order against RESPONDENT granting the relief requested by the Division in this Notice of Opportunity for Hearing.

Persons with a disability may request a reasonable accommodation such as a sign language interpreter, as well as request this document in an alternative format, by contacting Shelly M. Hood, ADA Coordinator, voice phone number 602/542-3931, e-mail [shood@cc.state.az.us](mailto:shood@cc.state.az.us). Requests should be made as early as possible to allow time to arrange the accommodation.

Dated this 29<sup>th</sup> day of March, 2001.



Mark Sendrow  
Director of Securities

# Memorandum

RECEIVED

DATE: March 29, 2001

2001 MAR 29 P 2: 27

TO: Nancy Cole  
Docket Control

AZ CORP COMMISSION  
DOCUMENT CONTROL

FROM: Amy Leeson  
Securities Division

RE: Stephen Michael Johnson  
Docket No. S-03403A-01-0000  
Assigned Staff

CC: Mabel Aldridge

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This is to notify you that the following individuals have been assigned to the above-mentioned case.

- ☒ Mark Sendrow
- ☐ LeRoy Johnson
- ☒ Matthew Neubert

Amy Leeson (Staff Attorney)

Lisa Busse (Staff Investigator)

**Note:** The Assistant Attorney General assigned to this matter is: Jennifer Boucek.